

Message Text

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ACTION EA-14

INFO OCT-01 ISO-00 SP-03 AID-20 EB-11 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 CIAE-00 COME-00 FRB-02 INR-10

NSAE-00 XMB-07 OPIC-12 LAB-06 SIL-01 DRC-01 /155 W
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R 111019Z JUL 74

FM AMEMBASSY MANILA

TO SECSTATE WASHDC 5152

INFO AMCONSUL HONG KONG

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E.O. 11652: N/A

TAGS: EFIN, RP

SUBJECT: CENTRAL BANK TAKEOVER OF CONTINENTAL BANK

REF: MANILA 7557

1. THE TAKEOVER OF CONTINENTAL BANK, THE COUNTRY'S EIGHTEENTH LARGEST COMMERCIAL BANK, BY THE CENTRAL BANK OF THE PHILIPPINES HAS GIVEN A MAJOR JOLT TO THE PHILIPPINE BANKING INDUSTRY. ALTHOUGH CONTINENTAL'S FAILURE WAS BASICALLY THE RESULT OF EMPLOYEE DEFALCATIONS, IT HAS EXPOSED SOME WEAKNESSES IN CENTRAL BANK SUPERVISION OF COMMERCIAL BANKS AND EMPHASIZED THE DANGERS OF THE LOOSE OPERATION OF THE PHILIPPINE MONEY MARKET.

2. CONTINENTAL BANK IS MEDIUM IN SIZE BY PHILIPPINE STANDARD WITH ASSETS OF ABOUT P530 MILLION. CB OFFICIALS HAVE INDICATED THAT BANK HAS MADE A NUMBER OF LOANS TO BANK OFFICERS OR THEIR NOMINEES WHICH ARE NOT BEING REPAYED. PRINCIPAL CULPRIT IS IDENTIFIED AS VICENTE T. TAN, EXECUTIVE VICE PRESIDENT OF THE BANK. ACCORDING
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TO BANKING SOURCES, TAN RIGGED LOANS TO NUMBER OF PARTIES

INCLUDING HIS PERSONAL SERVANTS AND USED FUNDS TO PURCHASE OTHER ASSETS INCLUDING SHARES IN PHILIPPINE TRUST COMPANY AND REAL ESTATE IN HAWAII.

3. GAME WAS UP WHEN CONTINENTAL WAS UNABLE REPAY HEAVY SHORT TERM MONEY MARKET BORROWINGS, VARIOUSLY REPORTED FROM P100 MILLION TO P300 MILLION. LATTER FIGURE EQUIVALENT TO TOTAL BORROWING AS OF MARCH 31ST REPORTED BY BANK. NUMBER OF PHILIPPINE COMMERCIAL BANKS AND MONEY MARKET INSTITUTIONS WERE DAMAGED BY CONTINENTAL FAILURE. BANCOM REPORTEDLY LOST P30 MILLION AND GENERAL BANK AND TRUST LOST HEAVILY ALSO. (GENERAL BANK'S RESULTING LIQUIDITY CRISIS HAS LED TO PURCHASE OF ITS SHARES BY DEVELOPMENT BANK OF PHILIPPINES WHICH BEING REPORTED SEPTTEL).

4. CONTINENTAL DEPOSITORS ARE RECEIVING FROM PHILIPPINE DEPOSIT INSURANCE CORPORATION RECOVERY OF DEPOSITS UP TO P10,000 MAXIMUM. HOWEVER, EXTENT OF REPAYMENT TO LARGER DEPOSITORS AND LENDERS WILL DEPEND ON CENTRAL BANK'S ABILITY RECOVER ASSETS OR OBTAIN LOAN REPAYMENTS.

5. THIS SITUATION HAS NATURALLY LED TO LOSS OF CONFIDENCE IN LOCAL BANKS, PARTICULARLY WEAKER ONES. CENTRAL BANK HAS STATED NO ADDITIONAL TAKEOVERS ARE BELIEVED TO BE NECESSARY AND IS MOVING IN NUMBER OF WAYS TO DISCOURAGE BANKS FROM RELIANCE ON MONEY MARKET FOR LENDING ASSETS. MOST IMPORTANT OF THESE IS TO LINK CB REDISCOUNTING PRIVILEGES TO BANKS' RESERVE POSITIONS, REWARDING BANKS WITHOUT EXCESSIVE DEFICIENCIES WITH INTEREST FREE FUNDS. THE CB HAS ALSO PROHIBITED MONEY MARKET INSTITUTIONS WITH CHRONIC RESERVE DEFICITS FROM LENDING FOR A TWO MONTHS PERIOD.

6. BANKING COMMUNITY HERE IS PREDICTABLY UNHAPPY ABOUT LOSS OF PUBLIC CONFIDENCE IN BANKS AND SPATE OF WITHDRAWALS AT WEAKER BANKS. HOWEVER, MOOD IN PRIVATE AND OFFICIAL CIRCLES APPEARS TO BE THAT SOME TIGHTENING OF REGULATIONS AND OF THE PRACTICES LIMITED OFFICIAL USE

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OF COMMERCIAL BANKS AND OF MONEY MARKET INSTITUTIONS IS NECESSARY TO THE LONG-RUN HEALTH OF THE INDUSTRY. THIS TIGHTENING PROCESS WILL BE MOST DIFFICULT FOR THE SMALLER COMMERCIAL BANKS AND THOSE WITH UNSOUND PRACTICES, BUT THESE BANKS ARE REGARDED AS VIABLE IF CENTRAL BANK SUPPORT FOR THEM IS CONTINUED.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: BLOCKED ASSETS, BANK LAW, BANK LOANS, BANK SERVICES
Control Number: n/a
Copy: SINGLE
Draft Date: 11 JUL 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: martinml
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974MANILA08301
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D740185-0233
From: MANILA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19740758/aaaabxmj.tel
Line Count: 114
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: MANILA 7557
Review Action: RELEASED, APPROVED
Review Authority: martinml
Review Comment: n/a
Review Content Flags:
Review Date: 23 JUL 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <23 JUL 2002 by shawdg>; APPROVED <26 FEB 2003 by martinml>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: CENTRAL BANK TAKEOVER OF CONTINENTAL BANK
TAGS: EFIN, RP, CENTRAL BANK, CONTINENTAL BANK
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005